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***Application of Harbor Island Utilities, Inc.
for approval of a new schedule of rates and charges
for water and sewer service provided to residential
and commercial customers in Harbor Island,
Beaufort County, SC***

Docket No. 2002-239-W/S

***Testimony of
Barbara J. Crawford
Audit Department***

Public Service Commission of South Carolina

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1 Q. PLEASE STATE FOR THE RECORD YOUR NAME, BUSINESS ADDRESS
2 AND POSITION WITH THE PUBLIC SERVICE COMMISSION OF SOUTH
3 CAROLINA.

4 A. My name is Barbara J. Crawford. My business address is
5 101 Executive Center Drive, Columbia, South Carolina. I
6 am employed by the Public Service Commission of South
7 Carolina as an Auditor.

8 Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND YOUR
9 EXPERIENCE.

10 A. I received a B.S. Degree in Business Administration with
11 a major in Accounting from the University of South
12 Carolina in 1979. I am a Certified Public Accountant,
13 licensed in the State of South Carolina. I am also a
14 Certified Internal Auditor. I have more than nineteen
15 years of audit experience, three of which have involved
16 the ratemaking process.

17 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY INVOLVING HARBOR
18 ISLAND UTILITIES, INC.?

19 A. The purpose of my testimony is to set forth in summary
20 form Staff's findings and recommendations resulting from
21 our examination concerning the above docket. These
22 findings and recommendations are set forth in the report
23 of the Audit Department with attached exhibits.

1 Q. I SHOW YOU THIS REPORT WITH ITS ATTACHED EXHIBITS,
2 ENTITLED "REPORT OF THE AUDIT DEPARTMENT, THE PUBLIC
3 SERVICE COMMISSION OF SOUTH CAROLINA, DOCKET NO. 2002-
4 239-W/S, HARBOR ISLAND UTILITIES, INC." DID YOU AND THE
5 AUDIT STAFF PREPARE THIS DOCUMENT?

6 A. Yes, the report was prepared by members of the Audit
7 Department Staff and me.

8 Q. (MARK FOR IDENTIFICATION). WOULD YOU PLEASE SUMMARIZE
9 THE CONTENTS OF THIS REPORT?

10 A. As outlined in the report's index, pages 1 through 4
11 contain the Staff's analysis of the report, with the
12 remaining pages 5 through 18 containing the Audit
13 Staff's supporting exhibits. The major part of my
14 testimony will refer to Audit Exhibit A, entitled
15 Operating Experience and Operating Margin-Combined
16 Operations. Such Exhibit, as do all other of the Audit
17 Staff's exhibits, utilizes a test year ending October
18 31, 2001.

19 Q. DO YOU HAVE ANY FURTHER EXPLANATION OF EXHIBIT A?

20 A. Yes, I do. The Staff prepared the exhibit in compliance
21 with the Commission's standard procedures as to
22 calculating income and operating margin for water and

1 wastewater utilities. A brief description of exhibit A
2 is as follows:

3 Column (1): Presents the Company's combined water and
4 wastewater operations per the Company's filing as of the
5 end of the test period under review. Special emphasis is
6 placed on net income for return and operating margin.

7 Column (2): Presents combined water and wastewater
8 accounting and pro forma adjustments per the Staff for
9 the period under review.

10 Column (3): This column details the combined water and
11 sewer operations of the Company as adjusted by the Staff
12 prior to the effect of the proposed increase.

13 Column (4): This column presents the proposed increase
14 in water and sewer rates as computed by the Commission
15 Staff Utilities Department and the resulting adjustments
16 to expenses.

17 Column (5): This column presents the Company's
18 normalized test year on a combined water and sewer basis
19 after including the proposed increase.

20 Q. PLEASE ELABORATE ON THE CALCULATIONS IN EXHIBIT A.

21 A. As shown in column (1), using combined water and sewer
22 operations per the Company's filing, the Staff computed
23 a net operating loss for return of (\$62,120). The Staff

1 computed a combined water and sewer operating margin of
2 negative (24.46%).

3 Shown in Column (2) are the accounting and pro forma
4 adjustments proposed by the Staff on a combined water
5 and sewer basis.

6 In Column (3), as adjusted combined water and sewer
7 operations are presented. The Staff computed as adjusted
8 net operating income for return, including growth, of
9 \$24,551. The Staff computed the combined water and
10 sewer as adjusted operating margin to be 8.96%.

11 Column (4) presents the Staff's computation of the
12 Company's proposed water and sewer revenue increase of
13 \$73,401. The Staff increased other taxes, income taxes
14 and customer growth for the effect of the proposed
15 increase. The effect of the proposed increase on net
16 income for return was computed to be \$42,176.

17 Column (5) presents combined water and sewer operations
18 as adjusted to normalize the test year on a pro forma
19 basis and after the effect of the proposed increase. As
20 a result, the Staff computed net income for return of
21 \$66,727. The Staff computed an operating margin of
22 20.15%.

1 Q. WOULD YOU PLEASE BRIEFLY DESCRIBE THE OTHER AUDIT
2 EXHIBITS IN THE STAFF'S REPORT?

3 A. Exhibit A-W provides the Company's operating experience
4 and operating margin for the Company's water operations.
5 Exhibit A-S provides the Company's operating experience
6 and operating margin for the Company's Sewer Operations.
7 Exhibit A-1 details the combined water and sewer
8 accounting and pro forma adjustments made by the Staff
9 and/or the Company. Company and Staff adjustments are
10 compared in this exhibit with a brief description of
11 each adjustment.

12 Exhibit A-2 details the Staff's computation of the
13 Company's customer growth. The Staff performed the
14 growth calculations using the formula method as detailed
15 in Exhibit A-2. The exhibit presents growth for water
16 operations only. The number of water customers
17 increased from 382 to 390 during the test year, which
18 resulted in a growth factor of 1.0%. Such growth factor
19 was applied to water operations only. The number of
20 sewer customers remained constant at 354.

21 Exhibit A-3 provides a reconciliation of the net income
22 for return computed by the Company to the net income for
23 return contained in Staff's Exhibit A.

1 Audit Exhibit A-4 presents the Company's income
2 statement for the year ended October 31, 2001.

3 Audit Exhibit A-5 presents the company's balance sheet
4 as of October 31, 2001.

5 Q. WHICH ADJUSTMENTS ON EXHIBIT A-1 IN YOUR REPORT ARE THE
6 RESPONSIBILITY OF THE AUDIT DEPARTMENT?

7 A. The adjustments marked with an (A) are the
8 responsibility of the Audit Department witness and the
9 ones marked with a (U) are the responsibility of the
10 Utilities Department witness. The adjustments that
11 contain both an (A) and a (U) denote partial
12 responsibility of both departments.

13 Q. PLEASE EXPLAIN THE ACCOUNTING AND PRO FORMA ADJUSTMENTS
14 CONTAINED IN EXHIBIT A-1.

15 A. Adj. # 1 Annualize Revenues - Both the Staff and the
16 Company propose to annualize water and sewer revenues
17 based on a bill frequency analysis for the year 2001.
18 The Staff adjusted water revenues by \$24,375 and sewer
19 revenues by \$2,423. The Company adjusted water revenues
20 by \$6,995 and sewer revenues by \$2,423.

21 Adj. # 2 DHEC Safe Water Fee - Both the Staff and
22 Company propose to remove DHEC Recoupment Fees in the
23 amount of (\$1,614). The Department of Health and

1 Environmental Control (DHEC) has jurisdiction over such
2 fees. They are billed to the Company's customers as a
3 separate line item on the utility bill and are intended
4 to recover the cost of certain water testing functions
5 required by state law. The Staff and Company have
6 eliminated revenues of (\$1,614) and Staff has eliminated
7 the associated expenses of (\$1,614) from water
8 operations.

9 Adj. #3 Interest Earned - Both the Company and the Staff
10 propose an adjustment to remove the revenue amount of
11 (\$70) for interest earned since such income is not
12 regulated by the Commission. This adjustment allocates
13 (\$46) to water operations and (\$24) to sewer operations.

14 Adj. # 4 Late Charges - The Company proposes to reduce
15 revenues in the amount of (\$517) for late charges
16 earned. This adjustment was allocated (\$336) to water
17 operations and (\$181) to sewer operations. The Staff
18 does not propose to make this adjustment since late fees
19 should be included in the calculation for operating
20 margin. Late fees are approved by this Commission.

21 Adj. #5 Tap Fees The Staff and the Company propose to
22 remove tap fees in the amount of (\$5,092) from revenues.
23 The Staff also proposes to remove an equal amount from

1 expenses since the cost of the tap is equal to the tap
2 fee. This adjustment allocates (\$3,310) to water
3 operations and (\$1,782) to sewer operations.

4 Adj. # 6 Interest Expense The Staff proposes to remove
5 interest in the amount of (\$28,447) which was deducted
6 by the Company as an expense. Such interest expense was
7 paid for the purchase of treasury stock. Staff does not
8 recommend that such cost be included for ratemaking
9 purposes. This adjustment allocates (\$18,491) to water
10 operations and (\$9,956) to sewer operations.

11 Adj. # 7 Donations - The Staff and the Company propose
12 to remove a donation in the amount of (\$150) from
13 expenses. Donations are considered non-allowable for
14 ratemaking purposes. This adjustment reduces water
15 expenses in the amount of (\$98) and reduces sewer
16 expenses in the amount of (\$52).

17 Adj. # 8 Rate Case Expenses - The Company proposes to
18 amortize rate case expenses totaling \$3,000 over three
19 years. The Company proposes an adjustment in the amount
20 of \$1,000. The Staff did not include this expense
21 because it was an estimate. The Staff does not recognize
22 estimated costs. The Company's proposed adjustment

1 increased water expenses in the amount of \$650 and
2 increased sewer expenses in the amount of \$350.

3 Adj. # 9 Excess Operating Expenses - The Staff and the
4 Company propose to remove excess charges which were paid
5 for line location services. The Company has an
6 administration and operator services contract with the
7 Beaufort Group, LLC. Per the services contract, the
8 Beaufort Group will provide certain services at an
9 agreed upon charge. Per the contract, labor charges for
10 line location services were set at a charge of \$20 per
11 line. During the test year, the Beaufort Group charged
12 the Company an hourly rate for actual labor hours worked
13 to locate lines during the test year rather than the
14 agreed upon price of \$20 per line. The Staff and the
15 Company propose to remove a total of (\$960) from
16 operating expenses, which represents the difference
17 between the contract price for line location services
18 and the actual amount paid. This adjustment reduces
19 water expenses in the amount of (\$624) and sewer
20 expenses in the amount of (\$336).

21 Adj. # 10 Management Fees- Per the administration and
22 operator services contract with the Beaufort Group, the
23 Beaufort Group provides the Utility with certain

1 management services at an agreed upon price. The
2 Beaufort Group billed the Company for fees in excess of
3 the amounts agreed upon in the contract. The Staff and
4 Company propose to reduce management fees in the amount
5 of (\$3,500) which represents the amount overcharged by
6 the Beaufort Group. This adjustment reduces water
7 expenses by (\$2,275) and reduces sewer expenses in the
8 amount of (\$1,225).

9 Adj. # 11 Postage Expense - Per the service agreement
10 with the Beaufort Group, the Company is required to pay
11 postage for the mailing of monthly bills. During the
12 test year, the Company was not billed for such postage
13 by the management company. The Staff and the Company
14 propose to annualize postage expense by increasing
15 expenses in the amount of \$1,591. This adjustment
16 allocates \$1,034 to water operations and \$557 to sewer
17 operations.

18 Adj. # 12 Depreciation Expense - The Staff proposes to
19 annualize depreciation expense using year end plant in
20 service. Plant in Service was reduced by Contributed
21 Capital and Contributions in Aid of Construction (tap
22 fees) before depreciation expense was computed. The
23 Staff proposes to reduce depreciation expense in the

1 amount of (\$2,675). The Staff's adjustment allocates
2 (\$1,471) to water operations and (\$1,204) to sewer
3 operations. The Company does not propose an adjustment
4 to annualize depreciation expense. However, the Company
5 does propose to allocate depreciation expense in the
6 amount of (\$1,972) from the water operations to the
7 sewer operations.

8 Adj. # 13 Telephone Expense - During the test year the
9 Company deducted telephone expense for only nine months.
10 The Staff and the Company propose an adjustment in the
11 amount of \$263 in order to annualize telephone expenses.
12 This adjustment allocates \$171 to water operations and
13 \$92 to sewer operations.

14 Adj. # 14 Labor Charges - Per the administration and
15 operator services agreement, the Beaufort Group was to
16 provide a set number of labor hours per month in
17 performing maintenance work for a set monthly service
18 charge. The Company was to be billed for any additional
19 labor hours needed to provide excess services for the
20 Company. During the test year, the Company was charged
21 for work which should have been covered by the monthly
22 service charge. The Company and the Staff propose to
23 make an adjustment in the amount of (\$28,182) for the

1 amount of excess labor charges paid by the Company
2 during the test year. This adjustment allocates
3 (\$16,182) to water operations and (\$12,000) to sewer
4 operations.

5 Adj. # 15 Purchased Water - An analysis of water
6 purchases reflected that water had been lost in excess
7 of 10%. Both Staff and Company propose to reduce
8 purchased water expense by (\$6,017) in order to adjust
9 for the unaccounted for water.

10 Adj. #16 Estimated Debt Service - The Company proposes
11 an adjustment to expense the estimated debt service cost
12 to relocate a pipeline across a new bridge which will be
13 built at some time in the future. The Staff does not
14 propose to include this estimate. The Commission does
15 not recognize estimated costs. The cost of debt should
16 be based on embedded cost rates, capital structure and
17 rate base.

18 Adj. # 17 Operating Expense - Per the Company's
19 agreement with the Beaufort Group, LLC, the annual fee
20 for the Beaufort Group to provide certain administration
21 and operator services is set at an annual rate of
22 \$38,360. The Company had only expensed a total of
23 \$35,816. Therefore, the Staff and the Company propose

1 an adjustment in the amount of \$2,544 which represents
2 the difference in the amount owed per the service
3 agreement and the amount expensed in the test year.

4 Adj. # 18 Operator Services Expense Allocation - Both
5 Staff and Company propose to allocate a portion of
6 operator services expense from water operations to sewer
7 operations. The Staff and the Company propose an
8 allocation in the amount of \$8,226. This adjustment has
9 no effect on total expenses.

10 Adjustment # 19 Income Taxes - Staff computed income
11 taxes on an as adjusted basis. Staff used water and
12 sewer operating revenue less expenses to compute income
13 tax expense. The income tax expense adjustment was
14 \$2,451 for water operations and \$3,377 for sewer
15 operations for a total of \$5,828 for combined
16 operations.

17 Adjustment # 20 Refunds - The Company issued refunds
18 totaling \$135 during the test year. Such refunds are
19 possibly non-recurring. Therefore, the Staff and the
20 Company propose an adjustment in the amount of \$135 to
21 increase revenue by the amount of the refunds recorded
22 during the test year. This adjustment allocates \$88 to
23 water operations and \$47 to sewer operations.

1 Adjustment # 21 Proposed Revenue - Both Staff and
2 Company propose to adjust revenue for the effect of the
3 proposed rates and charges. Staff proposes to increase
4 water revenues by \$34,801 and to increase sewer revenues
5 in the amount of \$22,302. This results in a combined
6 revenue increase adjustment in the amount of \$57,103.
7 The Company proposes to increase water revenues in the
8 amount of \$52,181 and to increase sewer revenues in the
9 amount of \$21,220. This results in a combined revenue
10 increase in the amount of \$73,401.

11 Adjustment # 22 Proposed Increase Gross Receipts Taxes -
12 The Staff proposes to include the effect of the proposed
13 increase on gross receipts taxes. The current gross
14 receipts tax rate was used by the Staff to calculate
15 this expense. The Staff proposes to increase expenses
16 for water operations in the amount of \$166 and to
17 increase expenses for sewer operations in the amount of
18 \$106 for a total adjustment of \$272. The Company does
19 not propose an adjustment for gross receipts taxes.

20 Adjustment # 23 Proposed Increase Income Taxes - The
21 Staff computed income taxes associated with the proposed
22 increase in revenues. The Staff computed an adjustment
23 for income taxes in the amount of \$8,827 for water

1 operations and an adjustment in the amount of \$6,086 for
2 sewer operations. This resulted in a total adjustment
3 in the amount \$14,913 for income taxes on a combined
4 basis.

5 Adj. # 24 Proposed Increase Purchased Water - The
6 Company proposes to adjust purchased water expense in
7 the amount of \$717 to reflect customer growth. Staff
8 does not propose to make this adjustment. The Staff
9 computed growth in both revenue and expenses by applying
10 a growth factor to net operating income for water
11 operations only. This is due to the fact that sewer
12 operations had zero growth. The customer growth
13 adjustment (shown in exhibit A-2) covers growth for the
14 proposed increase.

15 Q. MS. CRAWFORD, DOES THIS CONCLUDE YOUR TESTIMONY?

16 A. Yes, it does.

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